INLAND
NATURAL GAS CO. LTD. *and wholly-owned subsidiary companies*

13TH ANNUAL REPORT 1965

Communities served: HUDSON HOPE, PORTAGE MOUNTAIN DAMSITE, CHETWYND, SHELLEY, PRINCE GEORGE, QUESNEL, WILLIAMS LAKE, LAC LA HACHE, 100 MILE HOUSE, MERRITT, SAVONA, KAMLOOPS, NORTH KAMLOOPS, BROCKLEHURST, VALLEYVIEW, ARMSTRONG, ENDERBY, SALMON ARM, CANOE, OYAMA, WINFIELD, RUTLAND, KELOWNA, OKANAGAN MISSION, GLENMORE, PENTICTON, SUMMERLAND, OKANAGAN FALLS, OLIVER, OSOYOOS, GRAND FORKS, ROSSLAND, TRAIL, TADANAC, WARFIELD, KINNAIRD, CASTLEGAR, ROBSON, NELSON.

INLAND NATURAL GAS CO. LTD. *and wholly-owned subsidiaries*

OFFICERS

John A. McMahon, *President*
Fred B. Brown, *Vice-President*
D. R. MacPhail, *Secretary*
W. D. Alexander, C.A., *Treasurer*

DIRECTORS

Norman R. Whittall, *Chairman of the Board, Vancouver, B.C.*
Fred B. Brown, *Vancouver, B.C.*
William Manson, *Vancouver, B.C.*
Cyrus H. McLean, *Vancouver, B.C.*
John A. McMahon, *Vancouver, B.C.*
H. J. S. Pearson, *Edmonton, Alberta*
John D. Taggart, Q.C., *Vancouver, B.C.*

HEAD OFFICE

Sixth Floor, Shell Oil Building,
1155 West Georgia Street, *Vancouver 5, B.C.*

REGISTRAR

Eastern & Chartered Trust Company, *Vancouver, B.C.*

TRANSFER AGENT

Eastern & Chartered Trust Company, *Vancouver - Calgary - Toronto - Montreal*

AUDITORS

Riddell, Stead, Graham & Hutchison, *Vancouver, B.C.*

WHOLLY-OWNED SUBSIDIARIES

PEACE RIVER TRANSMISSION COMPANY LIMITED
ST. JOHN GAS & OIL CO. LTD. (N.P.L)
CANADIAN NORTHERN OIL & GAS LTD. (N.P.L.) *(Sold April 30, 1965)*
GRANDE PRAIRIE TRANSMISSION CO. LTD.
INLAND DEVELOPMENT CO. LTD.
INLAND TRANSMISSION CO. LTD.

13th Annual Report for the fiscal year ended June 30, 1965.

SEVEN-YEAR SUMMARY OF OPERATIONS

	1965	1964	1963	1962	1961	1960	1959
Sales of Gas	$ 9,177,852	$ 8,077,144	$ 7,213,374	$ 6,518,540	$ 5,420,109	$ 4,391,616	$ 2,947,097
Salaries and Wages	991,269	963,576	916,564	716,479	655,348	676,884	988,096
Depreciation and Depletion	897,412	878,702	624,996	357,192	164,358	174,593	19,508
Interest on Borrowed Money	1,631,624	1,637,036	1,582,601	1,524,155	1,477,505	1,451,009	1,358,997
Property Taxes and Franchise Payments	453,468	388,100	327,165	294,937	223,191	166,629	135,597
Net Income	1,537,517	1,045,209	869,594	831,666	891,819	599,089	147,271
Net Income per Common Share	49c	28c	26c	25c	27c	13c	4c deficit
Preferred Dividends Declared	400,000	400,000	250,000	250,000	250,000	250,000	250,000
Common Dividends Declared	585,406	292,703					
Net Investment in Fixed Assets	1,919,631	1,597,766	2,109,769	1,170,774	1,355,773	1,227,899	2,757,357
Fixed Assets less Accumulated Depreciation and Depletion	36,013,779*	36,333,763	35,614,699	34,057,607	33,271,406	32,109,810	31,263,467
Natural Gas Sales—Mcf (Inland)	10,596,269	10,070,343	9,141,873	8,130,368	6,977,679	5,048,174	2,939,689
Maximum Daily Sendout—Mcf (Inland)	51,740	42,711	48,466	43,393	31,614	23,609	24,783
Average use for Residential and Commercial Customers (Mcf)							
Residential	120	112	110	121	110	121	115
Commercial	596	513	507	559	513	555	536
Miles of Company Owned Mains and Service Lines in use:							
Transmission Lines:							
Inland	408	400	393	391	390	386	385
Subsidiaries	102	102	102	102	96	96	96
Distribution Mains	496	457	433	393	375	356	340
Service Lines	385	351	319	282	253	220	183

*Reflects sale of Canadian Northern Oil & Gas Ltd.

Kamloops Pulp & Paper Co. Ltd. mill due to start production in latter part of 1965.

PRESIDENT'S REPORT

The fiscal year ending June 30, 1965 was an excellent one in every respect.

In this period more gas was sold to more customers than ever before. Net earnings increased $492,308 with quarterly dividends of 6¼c each being paid on the common shares. An increase of 2,274 customers in the interval July 1, 1964 - June 30, 1965 was recorded bringing the total number of customers to 25,472.

To assist shareholders in assessing the progress of their Company since it began to distribute natural gas in 1957, and to give them some idea as to future prospects, submitted herewith is a seven-year statistical review and a section "Looking Ahead".

During the past year Mr. Ernest B. Bull, Q.C., who was a Director of your Company since its inception, resigned following his appointment as a Justice of the British Columbia Court of Appeal. The Board of Directors is pleased to announce the appointment of Mr. John D. Taggart, Q.C., to fill this vacancy.

It goes without saying that good results could not be achieved without loyal and hard working employees and at this point I wish to record thanks on behalf of the shareholders and Board of Directors.

To conclude, I see no reason for an interruption in the Company's annual growth curve in light of the rapid industrialization in the interior of British Columbia and of the rate reduction recently announced by your Company which will render gas an even more competitive fuel.

Our annual meeting will be held in Vancouver on October 28, 1965.

J. McMahon

PRESIDENT

September 20, 1965

DIRECTORS' REPORT TO SHAREHOLDERS

The Board of Directors submits herewith the Thirteenth Annual Report of Inland Natural Gas Co. Ltd. and its subsidiaries for the year ended June 30, 1965.

METERS IN OPERATION

	YEAR ENDED JUNE 30				
	1965	1964	1963	1962	1961
Residential Meters	22,020	20,148	18,007	15,739	13,798
Commercial Meters	3,433	3,027	2,713	2,288	1,999
Industrial Meters	19*	23	23	20	14
	25,472	23,198	20,743	18,047	15,811

*Reduction due to reclassification of customers.

NATURAL GAS SALES — Mcf

	YEAR ENDED JUNE 30		
	1965	1964	INCREASE
Residential	2,539,573	2,127,394	412,179
Commercial	2,636,220	1,978,638	657,582
Industrial	5,420,476	5,964,311	(543,835)
	10,596,269	10,070,343	525,926

Residential and commercial sales increased 1,069,761,000 cubic feet in 1965 compared with an increase of 644,624,000 cubic feet in 1964. The decline in industrial sales was due mainly to B.C. Hydro and Power Authority's partial replacement of thermal power generated at Quesnel and Prince George by hydro-electric power.

FINANCIAL

Operating Revenue

Total operating revenue for the year ended June 30, 1965, increased by 13% to $9,712,974. Sales of natural gas increased by $1,100,708, up 14%.

Other operating revenue amounted to $144,607, up from $116,294, due mainly to a further increase in rentals received on Company-owned equipment and to income from the sale of equipment under the Company's instalment purchase plans.

Operating Expenses

Operating expenses for the year were $6,431,713, an increase of $613,293 over 1964 expenses. The major portion of this increase can be attributed to costs which are directly related to sales, such as cost of gas purchased and franchise payments to municipalities.

Net Income

Net income for the year was $1,537,517, an increase of $492,308 compared with 1964. After payment of preferred dividends, earnings per common share amounted to 49c, compared with 28c in 1964.

Sinking Fund

First mortgage sinking fund bonds totalling $347,000 are due for retirement May 1, 1966. Debentures have already been purchased to satisfy the 1966 sinking fund requirements on the 5½% convertible debentures.

Dividends

Dividends of $1.00 per share were paid during 1965 on the 400,000 outstanding 5% cumulative redeemable preference shares. Dividends of 25 cents per share were paid on the common shares amounting to $585,406.

SOURCE AND APPLICATION OF FUNDS

The following statement shows the source and application of funds for the year 1965 on a consolidated basis.

Source of Funds		
Net income for the year	$1,537,517	
Add—Non cash charges to income		
Depreciation and depletion	897,412	
Amortization of discount and expense of funded debt	97,215	$2,532,144
Sale of investment in subsidiary company	1,315,000	
Less—Commission and expenses	74,833	1,240,167
		3,772,311
Application of Funds		
Additions to property, plant and equipment (net)	1,919,631	
Increase in mortgages and other long term receivables, less deferred income component	55,950	
Purchase of debentures for sinking fund	300,000	
Bonds redeemable within one year	347,000	
Dividends on preference and common shares	985,406	3,607,987
Increase in working capital		164,324
Working capital July 1, 1964		793,190
Working capital June 30, 1965		$ 957,514

Inland's Operations and Construction Headquarters in Prince George.

The school at Hudson Hope which soon will be converted to natural gas heating.

SHAREHOLDERS

As of June 30, 1965, there were 2,341,625 common shares outstanding. Common shareholders numbered 3,557 and there were 2,723 preferred shareholders. Geographical distribution of registered shareholders was:

Canada 90.7%   United States 8.0%   Other 1.3%

All the securities which have been issued by the Company are payable in Canadian funds only.

CAPITAL FORECAST FOR THE YEAR ENDING JUNE 30, 1966

The proposed capital budget for the year ending June 30, 1966 amounts to approximately $2,600,000. This will be the largest expenditure in several years and points up the continuing growth in British Columbia's Interior. Proposed special projects include a 3.8 mile 6″ line to Northwood Pulp Limited; a second feed to the City of Prince George through the P.G.E. Industrial Park; a 6″ lateral to Kamloops Pulp & Paper Co. Ltd., and an extension to Robson, near Castlegar. Also underway are extensions to the Peace River power plant site and to the community of Hudson Hope. A new sales and service centre is planned for Prince George.

WAGE AGREEMENTS

In January, the Office and Technical Employees' Union was certified as bargaining agent for office and technical employees in Vancouver and in the field offices. Negotiations have been carried on for several months, but no formal agreement has yet been signed. Negotiations with the International Brotherhood of Electrical Workers are under way, the

Pentícton Sales & Service Office.

present agreement having terminated on September 12th. This agreement covers customer service and operations and construction workers.

INDUSTRIAL CONTRACTS

Contracts for large blocks of firm or interruptible natural gas have been entered into with Kamloops Pulp & Paper Co. Ltd., Prince George Pulp and Paper Limited and Northwood Pulp Limited. It is anticipated that the mill at Kamloops will begin production during the latter part of 1965 while it is not expected that the other mills will begin production until the second quarter of the calendar year 1966. These contracts combined provide for maximum daily deliveries by our Company of 21 million cubic feet per day.

SALES ACTIVITIES

Your Company has carried on an aggressive sales campaign through the promotion of gas appliances. We now offer, through various long-term finance and lease plans, a wide variety of gas-fired appliances, including conversion burners, space heaters, water heaters, unit heaters, gravity and forced-air furnaces, ranges, dryers and fireplaces. These appliances are available to residential or commercial users and at this date over 6,000 have been installed. The appliance program has enabled us to convert a good percentage of existing buildings to natural gas. 46.2% of all customers added during the year under review were in existing premises. New construction has continued at an increasing rate and the Company continued to attach over 90% of this construction to our mains.

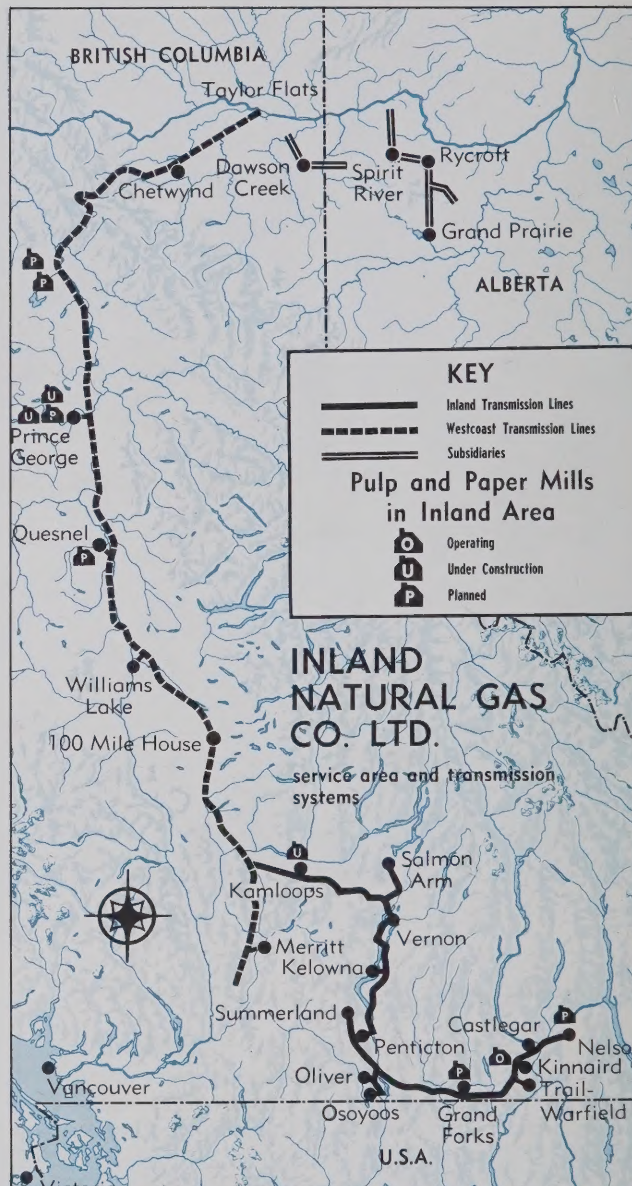
It has been a very successful year for converting schools to natural gas with conversions taking place or scheduled early in the fall at Nelson, Castlegar, Trail, Osoyoos, Oliver, Penticton, Summerland, Vernon and Kamloops. The total number of schools now using natural gas in our system is 123. This represents nearly every school in our distribution area. With the rapid population growth in all communities that we serve, new schools are planned in almost every community and we look forward to the trend of natural gas acceptance by school boards continuing.

With the increase of tourist trade in the Province due to new highway construction, there has been a rapid expansion in buildings to increase tourist accommodation.

We have been extremely successful in attracting these new facilities and now have 150 apartment buildings, 192 motels and 78 hotels using natural gas. Other commercial and industrial users at a high saturation include 22 hospitals and 24 sawmills.

LOOKING AHEAD

Prince George is thought to be among the fastest growing industrial areas in Canada. Under construction are pulp mills, sawmills, apartments, housing projects, office buildings, hotels and shopping centres.



Pulp and Paper Mills in Inland's Territory.

It is also the chief supply point for the Peace River hydro-electric development which is under construction at Portage Mountain.

About twelve hundred men are employed in construction of the Prince George Pulp and Paper mill and it is expected that when this mill is completed in the spring of 1966 the same crews will be retained to construct Intercontinental's pulp mill which is adjacent to the Prince George pulp mill. Union Oil Company has announced plans to build a five million dollar refinery. There is a two million dollar hotel and a one million dollar apartment block nearing completion. Woodward's, a leading department store, are building a four million dollar shopping centre. Airport runways are being extended and a one million dollar air terminal has been announced. The Pacific Great Eastern Railway is developing an indus-

trial park in South Prince George and to date fifty-three industrial applications (involving thirty-five million dollars in private capital investment) within the industrial park have been approved.

The Kamloops area is another participant in British Columbia's booming economy. The Kamloops Pulp & Paper Co. Ltd. are scheduling their plant to be in production by late fall of 1965. In addition this company has already announced that it is studying expansion plans. Housing projects, apartment blocks, hotels, shopping centres are also under construction in this region.

The Okanagan Valley, because of its many facilities and proximity to major population centres, can anticipate continued expansion in the tourist trade. The opening of the Rogers Pass section of the Trans-Canada Highway has not only brought Prairie markets much closer but has also considerably swelled the influx of visitors. The tourist trade will receive yet another lift when the highway through the Yellowhead Pass is completed, as this will establish a link with Edmonton.

On September 16, 1964, the Columbia River Treaty involving Canada and the United States was signed. It is estimated that one billion dollars will be spent during the next twenty years on ten Columbia River power projects. Impact from the construction and payrolls (which are expected to total thirty-five million dollars) of Arrow, Duncan, Murphy, Bonnington, Brilliant, Kootenay, Canal, and Seven Mile projects will be felt in the West Kootenay area, which includes Trail, Castlegar, Kinnaird, and Nelson, where your Company has an extensive distribution system.

RATE REDUCTION AND REGULATION

In 1960, three years after your Company had commenced distributing natural gas, the Public Utilities Commission ordered a public hearing to review the Company's natural gas rates. The rates were found to be "satisfactorily designed to provide the public with maximum service at the lowest rates consistent with presently increasing and ultimately sufficient Company earnings."

Since the Hearing in 1960 there has been a marked growth in both population and industry in your Company's franchised area. With a sound base for a continuation of this growth as indicated elsewhere in this report, the Company has proposed a rate reduction so that the consumers can share in the Company's progress. The reduction will assist in promoting new business and increasing consumption by existing customers and thereby improve the long-term interest of the shareholders.

The rate reduction that the Company proposes is to be implemented over a three-year period and the estimated total savings that will accrue to residential and commercial customers will be approximately one million dollars. Before the reduction can become effective, there will be a public inquiry to be held this autumn before the Public Utilities Commission.

CANADIAN NORTHERN OIL & GAS LTD. (N.P.L.)

It is our estimate that Inland's utility operations will require something in the order of 7½ million dollars over the next three years to meet demands for new services; moreover, in the years immediately following an even greater capital outlay will be needed to increase the capacity of the present system. In planning the financing we reviewed your Company's investment in Canadian Northern Oil and Gas Ltd. to see if the funds could be more profitably employed in the utility system. The services of McDaniel Consultants (1965) Ltd., Calgary, specialists in oil and gas reservoir evaluations, were engaged to make an appraisal and evaluation of the Company's gas and oil reserves. As a result of their findings, the decision to dispose of Canadian Northern was reached. Their report placed a value of $1,087,730 on the gas and oil reserves and the undeveloped land, and an estimated income tax benefit applicable to future years of $273,000.

Your Company then engaged the services of Charles R. Hetherington & Co. Ltd., Calgary, a firm of consulting engineers, to promote sale of Canadian Northern. They were successful in developing an interest among a number of Canadian oil companies and a firm bid of $1,315,000, submitted by Canadian Industrial Gas & Oil Ltd., was accepted, to be effective April 30, 1965. The financial statements reflect this sale.

ST. JOHN GAS & OIL CO. LTD. (N.P.L.)
(a wholly-owned subsidiary)

Lease selections from former permits 22 and 30 near Fort St. John, B.C.

Production of gas amounted to 40.1 million cubic feet, down from 40.5 million cubic feet in 1964.

PEACE RIVER TRANSMISSION COMPANY LIMITED
(a wholly-owned subsidiary)

Sales to Northland Utilities Limited for the distribution of natural gas in Dawson Creek and Pouce Coupe amounted to 1,680 million cubic feet compared with 1,585 million cubic feet in 1964.

GRANDE PRAIRIE TRANSMISSION CO. LTD.
(a wholly-owned subsidiary)

Total sales in 1964 amounted to 1,078 million cubic feet compared to 857 million cubic feet in 1964.

For the Board of Directors,

PRESIDENT

September 20, 1965

CONSOLIDATED BALANCE SHEET
AS AT JUNE 30, 1965

(with comparative figures for the prior year)

ASSETS

	1965	1964
CURRENT ASSETS		
Cash	$ —	$ 190,922
Marketable securities, at cost (market value 1965 – $203,600)	204,192	599,660
Accounts receivable less allowance for doubtful accounts	837,364	713,072
Due on sale of investment in subsidiary company	1,315,000	—
Inventories of materials and supplies, at cost	580,486	484,906
Prepaid expenses	22,588	30,795
Total current assets	2,959,630	2,019,355
MORTGAGES AND OTHER LONG TERM RECEIVABLES	408,168	331,299
PROPERTY, PLANT AND EQUIPMENT, at cost		
Natural gas transmission lines and distribution systems	35,265,477	33,893,694
Plant, buildings and equipment	2,279,352	2,423,989
	37,544,829	36,317,683
Less – Accumulated depreciation	2,914,014	2,451,945
	34,630,815	33,865,738
Interest in petroleum and natural gas licenses, permits and reservations, including development thereon		
Producing properties	69,230	1,656,550
Less – Accumulated depletion	22,071	520,884
	47,159	1,135,666
Non producing properties	367,104	426,932
	414,263	1,562,598
Land and land rights	968,701	905,427
	36,013,779	36,333,763
OTHER ASSETS AND DEFERRED CHARGES		
Commission and expense on issue of preference shares	1,265,678	1,265,678
Unamortized discount and expense on funded debt	1,622,029	1,719,244
Incorporation and organization expenses	23,514	101,628
Excess of cost of shares of subsidiary companies over book value of such subsidiaries at date of acquisition	—	168,497
	2,911,221	3,255,047
	$42,292,798	$41,939,464

LIABILITIES

	1965	1964
CURRENT LIABILITIES		
Bank loan and overdraft	$ 122,561	$ —
Accounts payable	701,308	465,845
Interest accrued on funded debt	337,705	343,778
Dividends payable	100,000	100,000
Estimated income taxes payable	18,555	8,195
Property and franchise taxes accrued	374,987	308,347
Bonds redeemable within one year	347,000	—
Total current liabilities	2,002,116	1,226,165
DEFERRED INCOME	117,791	96,872
FUNDED DEBT		
First Mortgage Sinking Fund Bonds		
6¼% Series C, maturing May 1, 1983	20,000,000	20,000,000
Less included in current liabilities	347,000	—
	19,653,000	20,000,000
5½% Convertible Sinking Fund Debentures, Series A, maturing February 15, 1977 (Note 2)	6,500,000	6,800,000
	26,153,000	26,800,000
SHARE CAPITAL AND SURPLUS		
Share capital (Note 3)		
5% Cumulative redeemable preference shares, par value $20 per share		
Authorized: 500,000 shares		
Issued: 400,000 shares	8,000,000	8,000,000
Common shares, par value $1 per share		
Authorized: 5,000,000 shares		
Issued: 2,341,625 shares	2,341,625	2,341,625
Premium on common shares issued	1,158,745	1,158,745
Earned surplus per statement attached	2,519,521	2,316,057
	14,019,891	13,816,427
	$42,292,798	$41,939,464

Approved on behalf of the Board

JOHN A. McMAHON, Director

FRED B. BROWN, Director

The accompanying notes to financial statements are an integral part of the above consolidated balance sheet.

INLAND NATURAL GAS CO. LTD. *and wholly-owned subsidiaries*

STATEMENT OF CONSOLIDATED INCOME AND EARNED SURPLUS FOR THE YEAR ENDED JUNE 30, 1965 *(with comparative figures for the prior year)*

	1965	1964
OPERATING REVENUE		
Sale of gas	$9,177,852	$8,077,144
Transportation allowance	175,656	151,800
Oil and natural gas production	167,542	212,070
Connection charges	47,317	41,570
Other operating revenue	144,607	116,294
	9,712,974	8,598,878
OPERATING EXPENSES		
Purchase of gas	3,847,523	3,464,103
Operation and maintenance of transmission and distribution systems	819,635	736,260
Operation of producing properties, including depletion of $38,936 – 1965; $44,332 – 1964	83,665	90,551
Provincial and municipal taxes	277,578	240,160
Franchise expense	175,890	147,940
General and administrative expenses	368,946	305,036
Provision for depreciation	858,476	834,370
	6,431,713	5,818,420
Income from operations	3,281,261	2,780,458
OTHER INCOME		
Income from investments	19,749	34,323
	3,301,010	2,814,781
OTHER DEDUCTIONS		
Interest on borrowed money	1,631,624	1,637,036
Amortization of discount and expense of funded debt	97,215	97,130
Loss on disposal of fixed assets	—	4,588
	1,728,839	1,738,754
Income before taxes thereon	1,572,171	1,076,027
Provision for income taxes (Note 4)	34,654	30,818
NET INCOME for the year	1,537,517	1,045,209
Earned surplus at beginning of year	2,316,057	1,963,551
	3,853,574	3,008,760
Deduct		
Dividends declared on preference shares	400,000	400,000
Dividends declared on common shares	585,406	292,703
Loss on sale of investment in Canadian Northern Oil and Gas Ltd. (N.P.L.)	348,647	—
	1,334,053	692,703
EARNED SURPLUS at end of year	$2,519,521	$2,316,057

The accompanying notes to financial statements are an integral part of the above statement of consolidated income and earned surplus.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

As at June 30, 1965

1. PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of Inland Natural Gas Co. Ltd. and all wholly-owned subsidiary companies as at June 30, 1965. Canadian Northern Oil & Gas Ltd. (N.P.L.), a wholly-owned subsidiary company, was sold effective April 30, 1965 and the statement of consolidated income and earned surplus includes the revenues and expenses of that company to date of sale.

2. 5½% CONVERTIBLE SINKING FUND DEBENTURES

The 5½% Convertible Sinking Fund Debentures, Series A are (inter alia) unsecured obligations of the Company but are subject to restrictions of the Trust Indenture dated February 15, 1957. They are callable at a premium of 3.1% up to and including February 14, 1966 and thereafter at a reducing premium. The debenture holders have the option to convert each debenture at any time up to 2:00 p.m. (P.S.T.) on November 15, 1967, into fully paid and non-assessable Common Shares in the capital stock of the Company at the principal amount of the debenture without adjustment for interest thereon at the following prices per share: on or before November 15, 1965 — $14.75, thereafter and on or before November 15, 1966 — $16.00, and thereafter and before 2:00 p.m. (P.S.T.) on November 15, 1967 — $17.25.

3. COMMON SHARE PURCHASE WARRANTS

There are purchase warrants outstanding entitling the holders thereof to purchase 248,925 Common Shares of the Company up to 2:00 p.m. (P.S.T.) on November 15, 1966, at the following prices per share: on or before November 15, 1965 — $14.75, and thereafter and before 2:00 p.m. (P.S.T.) on November 15, 1966 — $16.00.

4. INCOME TAXES

The Company and its subsidiaries, Peace River Transmission Company Limited and Grande Prairie Transmission Co. Ltd. are claiming capital cost allowances for income tax purposes which are in excess of the depreciation recorded in their accounts and the provision for income taxes is approximately $500,000 less than the provision that would otherwise have been charged against income for the year ended June 30, 1965. The accumulated amount by which income taxes have been so reduced in this and prior years is approximately $2,215,000. This policy may be expected to result in a situation in future years wherein capital cost allowances which may be claimed for tax purposes may under certain circumstances be less than depreciation recorded in the Companies' accounts with a consequent increased tax burden in such years.

In September 1964 the Public Utilities Commission changed its method of calculating income taxes in the regulation of natural gas companies in order that the savings resulting from the use of capital cost allowances in excess of depreciation provided would flow through to the consumers. For regulatory purposes only, the total tax differential accumulated by the Commission is being credited to income tax expense at the rate of approximately $160,000 per annum plus interest for the fiscal years 1964 to 1968 inclusive. No change is required in the Company's accounts which, as approved by the Commission, do reflect the "flow-through" basis for income taxes.

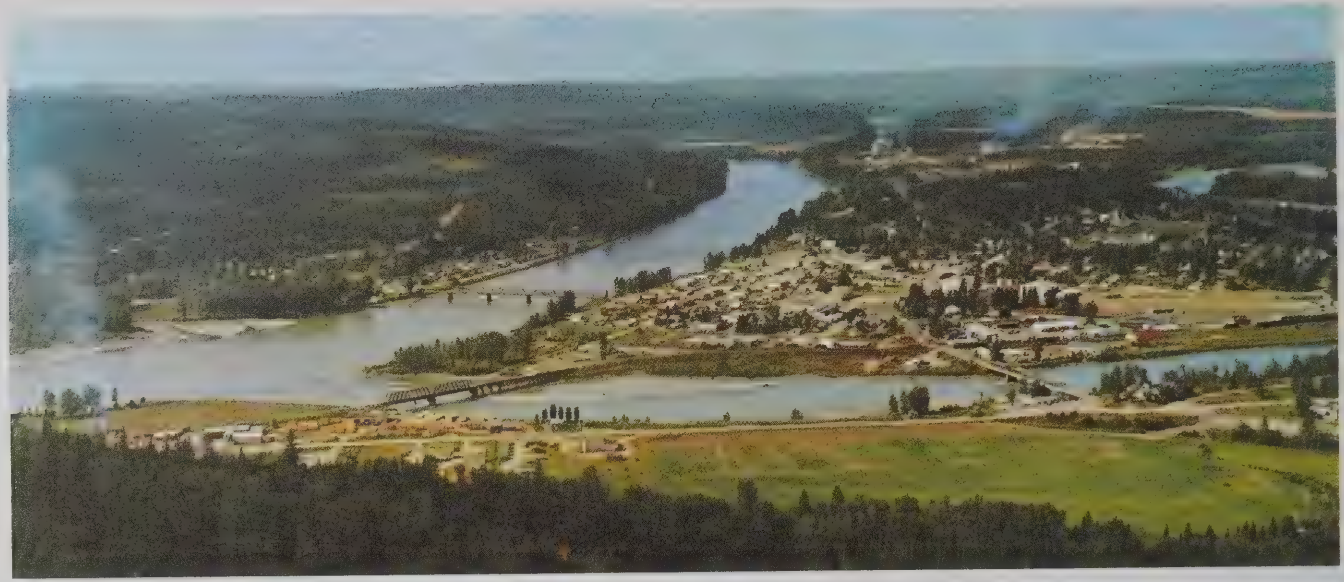
AUDITORS' REPORT TO THE SHAREHOLDERS

We have examined the consolidated balance sheet of Inland Natural Gas Co. Ltd. and its wholly-owned subsidiary companies as at June 30, 1965 and the statement of consolidated income and earned surplus for the year then ended and have obtained all the information and explanations we have required. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion, the accompanying consolidated balance sheet and statement of consolidated income and earned surplus are properly drawn up in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year and together with the notes thereto present fairly the financial position of Inland Natural Gas Co. Ltd. and its wholly-owned subsidiary companies as at June 30, 1965 and the results of their combined operations for the year then ended according to the best of our information and the explanations given to us and as shown by the books of the companies.

Vancouver, B.C.,
August 20, 1965.

RIDDELL, STEAD, GRAHAM & HUTCHISON
Chartered Accountants.



Town of Quesnel, largest of the Cariboo communities.

Vernon Jubilee Hospital, one of the many hospitals using natural gas.

A new motel in Vernon using natural gas.

The nearly completed Fort George Hotel, Prince George, which will fully utilize natural gas.

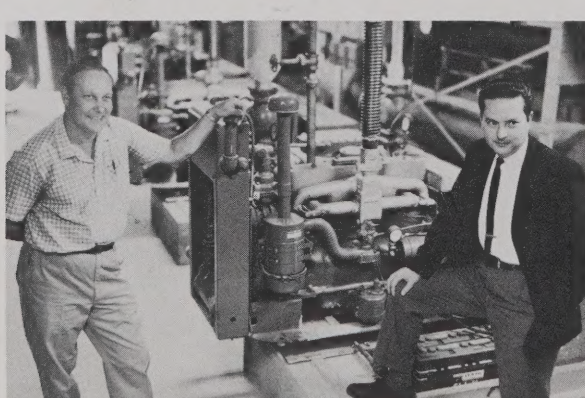
Village of Salmon Arm, situated on the Trans-Canada Highway.

natural gas scores another first!

British Columbia's first natural gas-powered rink refrigeration system goes into operation this month with the inauguration of North Kamloops' exciting new Sports Centre.

Year-round refrigeration of the centre's 90′ x 195′, 150-seat skating rink and 6 sheets of curling ice (with provision for 4 more) called for dependable and economical power. Comparative studies of power systems and equipment indicated substantial operating economies with natural gas engines, plus long-term dependability of operation and supply.

Inland Natural Gas Co. Ltd., as fuel supplier to this project, is proud to be associated with another trend-setting development in the utilization of natural gas.



Architect E. A. Mulford of Kamloops (right) discusses installation of the natural gas engines with George H. Williams, General Superintendent of Burrard Refrigeration and Air Conditioning Co. Ltd. of Vancouver. Consulting Engineers were Phillips Barratt & Partners of Vancouver.

Inland NATURAL GAS CO. LTD.

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